

Chapter 10 – Capitalized Software

Introduction Software capitalization

In FY 2001, the Service implemented their software capitalization policy through the memorandum dated July 9, 2001 from the Acting Deputy Director. See Appendix 6, 149. The policy instructs the Service programs to capture software development costs using a FFS project number.

POLICY Software capitalization

Under the Service software capitalization policy, if the Service incurs \$100,000 or more in cumulative costs to purchase and implement software, and the software is considered to have a useful life of more than 2 years. The cost should be capitalized. For existing software, costs should only be capitalized if the cost is equal to or greater than \$100,000 and is considered an enhanced version to the system. Minor enhancements or ongoing maintenance to a system are not subject to capitalization. In addition, bulk purchases of software should not be capitalized if the unit cost or per license fee is less than \$100,000.


GUIDANCE Software capitalized costs

Capitalized costs should include amounts paid to:

- Vendors for commercially purchased software;
- Contractors or employees to implement and install the commercially purchased software;
- Contractors or employees to design, program, install and implement internally developed software.

PROCEDURE Software capitalized accounting procedure

Program and Regional offices must follow existing Service policy requiring acquisition requests for information technology (IT), including software, to be reviewed and approved by program and Regional Chief Technology Officers (CTO). Once approved and the software project manager from the program or Regional office determines its internal use software development project or modification to existing software meets capitalization criteria,

Step	Action
1	The project manager will request a FFS project number from the Cost Accounting Section within Division of Financial Management (DFM). The Cost Accounting Section sets a project number in FFS.
2	The project manager will then notify their CTO and DFM – Washington office that the office has established a project number to track the software costs.
3	Each quarter, DFM will provide the project manager all FFS transactions and cost incurred during the quarter.
4	The project manager will review the transactions to ensure all costs within that project number should be capitalized and provide the information to DFM.
5	DFM ensures that the costs are posted to the applicable general ledger account. Refer to guidance and example of the accounting process flow.
	Complete.

The above process continues until final acceptance testing has been successfully completed. At the same time:

Step	Action
1	The project manager will notify DFM – Washington office of the acceptance date.
2	DFM will provide the project manager all FFS transactions and cost incurred up to the acceptance date.
3	The project manager will perform a final review of costs and provide the information to DFM. Costs incurred after the acceptance date should be expensed.
4	The project manager will provide the expected useful life of the software to DFM.
5	The project manager will notify their CTO and Division of Contracting and Facilities Management (CFM) that the software project has been accepted.
7	The project manager will provide the software asset information, including expected useful life, to CFM for entering in the Personal Property Management System (PPMS). 👉 The acquisition cost shown in PPMS must agree with the cost capitalized in FFS.
8	DFM will ensure the costs are posted to applicable FFS accounts and start amortizing the costs over the software's expected useful life.
9	The project manager will notify their CTO and DFM of any changes in the asset's useful life.
👍	Complete.

GUIDANCE

Software
capitalized
accounting flow

The software capitalization project costs will be moved at least quarterly to the Internal Use Software-in-Development (1832) Standard General Ledger (SGL) Account. The software capitalization policy requires indirect cost to be allocated to the cost of the capitalized software. Since software development is predominantly contracted work, the principle additive costs are acquisition and financial management. Other indirect costs remain relatively fixed. Therefore, the Service will apply its pass-through cost recovery rate to the expenses transferred to the Software-in-Development SGL Account. This rate was designed to recover acquisition and financial management costs.

Treasury has created two “counter-expense” SGL accounts to provide a mechanism for transferring direct and indirect expenses to an asset account. The following example adopts Treasury’s Approved Scenario for Internal-Use Software and provides the process flow to be used. The below examples assume all apportionments, allotments, and obligations were made.

EXAMPLE

Scenarios
1-3:

Software
capitalized
accounting flow

The examples below show how to go through a software capitalized accounting process for Scenarios 1 to 3:

Scenario 1: The software project manager from the program determines its internal use software development project or modification to existing software meets capitalization criteria.

Step	Action
1	Project manager requests FFS project number from the DFM Denver Operations, Cost Accounting Section.
2	The Cost Accounting Section sets project number in FFS.
3	Program communicates to the DFM -Branch of National Policy and Financial Analysis that the project number is to capture capitalized software costs.
4	The Branch of National Policy and Analysis notifies the DFM - Branch of Financial Statements of the capitalized software project numbers.

Scenario 2: Program records payroll and other direct cost to FFS project code related to internal Software-in-Development.

1	The Accounting Entry below assumes obligation was already made.			
	Accounting Entry			
	6100	Program Expenses 1010. Fund Balance with Treasury	100,000	100,000
	3100	Unexpended Appropriation 5700. Appropriation Used	100,000	100,000
	4801	Undelivered Orders – Obligations, Unpaid 4902. Delivered Orders – Paid	100,000	100,000
👍	Complete.			

Scenario 3: At least quarterly, the project manager reviews the FFS transactions and identifies the transactions and capitalized costs. DFM reclassifies the identified transactions from expenses to a software-in-development asset.

1	Accounting Entry			
	1832	Internal Use Software-in-Development 6600. Applied Overhead 6610. Direct Cost Capitalization Offset	104,500	4,500 100,000
👍	Complete.			

EXAMPLE
Scenarios
4-6:

Software
capitalized
accounting flow


The examples below show how to go through a software capitalized accounting process for different scenarios 4 to 6:

Scenario 4: The project manager notifies DFM that software was brought “in production.”

Step	Action			
1	DFM provides project manager final review of quarterly costs and current capitalized in development costs.			
2	The project manager reviews final transactions and confirms final capitalized costs.			
4	DFM ensures costs are posted to applicable SGL accounts.			
	Accounting Entry			
	1832	Internal Use Software-in-Development 6600. Applied Overhead 6610. Direct Cost Capitalization Offset	20,900	900 20,000
	1830	Internal Use Software 1832. Internal Use Software-in-Development	125,400	125,400
👍	Complete.			


Scenario 5: DFM amortizes the “in-production” software over the expected useful life.

Accounting Entry

1	6710	Depreciation Expense	25,080	
	1839	Accumulated Amortization-Software		25,080
	Complete.			

Scenario 6: The project manager notifies DFM that new technology has rendered their software obsolete and the program will not realize any use from the software.

Accounting Entry

1	DFM adjust general ledger to reflect that asset is not part of operations and has no value.			
	7210	Losses on Disposal of Assets	100,320	
	1839	Accumulated Amortization – Software	25,080	
		1830. Internal Use Software		125,400
	Complete.			